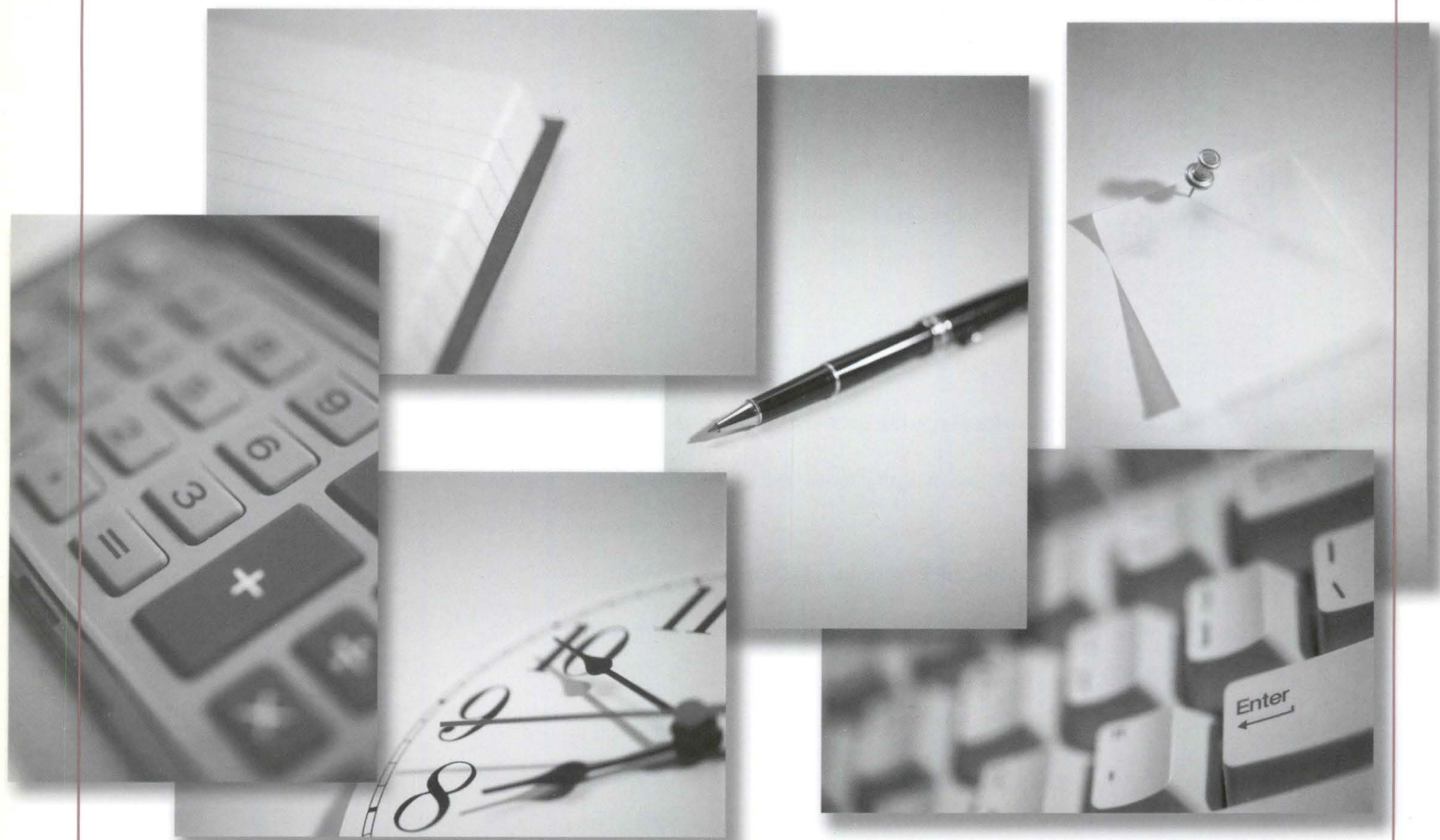




The Law Society of Upper Canada



Annual Report
2004

Financial Statements

ANNUAL GENERAL MEETING, 2005

Wednesday, May 11, 2005

at 5:15 p.m.

Osgoode Hall, Toronto

ORDER OF BUSINESS

Minutes of the previous Annual General Meeting

Report of the work of the Society and the committees
of Convocation

Presentation of the audited financial statements

Matters of professional interest that are related to the work
of the Society

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| LAWYERS FUND FOR CLIENT COMPENSATION | 17-23 |
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Management Discussion and Analysis

The Law Society of Upper Canada ("the Society") General Fund comprises its unrestricted fund, funds restricted by Convocation for special purposes and endowment funds held in trust. The Society's annual membership fee is based on the financial requirements of the restricted and unrestricted funds.

The unrestricted fund is the Society's operating fund representing the bulk of its revenues and expenses. The funds restricted by Convocation are the Capital Allocation, Invested in Capital Assets, County Libraries, Special Projects, Repayable Allowance, Endowments and the Working Capital Reserve.

BALANCE SHEET

Cash and short-term investments and portfolio investments

Cash and short-term investments have decreased by approximately \$4.0 million from 2003 to \$22.2 million. As approved by Convocation, \$10.0 million was transferred to a new long-term portfolio during the year. The short-term investments include government-backed securities and money market instruments issued by major Canadian banks.

Portfolio or long-term investments of \$10.1 million at the end of 2004 are invested in high quality fixed income (82%) and equity (18%) products. Fixed income investments comprise a diversified mix of government, provincial and corporate bonds with an investment rating of "BBB" or better. Equity investments comprise a diversified mix of equities listed on the New York and Toronto stock exchanges. The year-end market value of the portfolio is \$10.0 million.

Capital assets

The increase in capital assets from \$16.9 million to \$18.1 million reflects the start of the North Wing renovation project in September 2004.

Deferred revenue

Deferred revenue of \$6.9 million has increased by \$5.1 million from 2003. It is predominantly 2005 membership fees received in 2004.

Unclaimed trust funds

Unclaimed trust funds continue to increase reaching \$1 million in 2004, an increase of \$299,000. These are trust monies turned over to the Society by members who are unable to locate the persons to whom the monies are owed. By statute, the Society administers these funds, in perpetuity, with the net income from the funds transferred to the Law Foundation of Ontario annually.

STATEMENT OF REVENUES AND EXPENSES

The Society's unrestricted fund has generated a surplus of \$1.8 million as a result of operations for 2004. This is being used to finance operating expenses and therefore reduce membership fees in 2005. The surplus was

achieved largely as a result of greater than anticipated revenues, particularly Professional Development and Competence ("PD&C") revenues, corporate revenues such as cost recoveries by the enforcement unit, litigation cost recoveries, *Ontario Reports* royalties and fees for mobility applications. Net expenses for the year varied from budget by less than \$50,000.

Membership fees

Membership fees for 2004 are \$35.1 million, \$1.2 million greater than 2003 largely as a result of total membership increasing by almost 700 to 35,700.

Professional Development and Competence

PD&C revenues increased from \$11.3 million in 2003 to \$12.2 million in 2004. The major components of PD&C are the bar admission course ("BAC") and post-call education programs.

In 2004, the PD&C division continued the expansion of Law Society competence products. As well, attendance at post-call education programs continued to increase. Total program revenue increased \$500,000 from \$3.4 million in 2003 to \$3.9 million in 2004.

Total BAC revenues increased by \$310,000 to \$8.04 million, up from \$7.73 million in 2003. This was due to an increase in the support provided by the Law Foundation of Ontario and an increase in the number of students, generating an additional \$176,000 of tuition revenue. BAC tuition fees at \$4,400 have remained unchanged since 2001.

PD&C expenses increased approximately \$2.5 million to \$17 million. Major increases were attributable to:

- the development and implementation of the new licensing process to replace the current BAC.
- expenditures for the education administration system redesign.
- increased numbers of BAC students and increased uptake in post-call events, particularly at remote sites, resulting in higher costs for such major items as materials production, location and instructor costs. Increased revenues for the BAC and post-call programs largely offset these increased costs.

Professional Regulation

Professional Regulation expenses increased from \$9 million in 2003 to \$10 million in 2004. The current year saw the continuation of the business process changes, the selection of a new vendor to build a new case management system, the beginning of system development and full implementation of the Intake and Enforcement units.

A significant factor in the increase in expenditures is the cost of mortgage fraud investigations, particularly in retaining outside counsel and added staff. The mortgage fraud investigations continue to consume resources – the 2005 operating budget allocates \$1 million to directly address these types of investigations.

Investment income

Investment income decreased to \$3.8 million in 2004 from \$4 million in 2003. Overall the rate of return on all investments declined to 2.15% in 2004 from 2.87% in 2003 as investment yields declined over most of 2004 in line with interest rates.

General Fund

Other revenue

Other revenue of \$5 million includes a variety of items such as Lawyer Referral Service fees, *Ontario Reports* royalties, catering revenues, litigation and enforcement cost recoveries, charges for fee payment plans and other miscellaneous revenues. There were general increases in these categories resulting in other revenue increasing \$677,000 from 2003.

RESTRICTED FUNDS

Capital Allocation

The large balance in the Capital Allocation Fund of \$8.2 million (2003: \$9.4 million) reflects the transfers in prior years to finance the North Wing renovation commenced in 2004.

Invested in Capital Assets

The increase reflects the growth in capital assets from \$16.9 million to \$18.1 million as a result of the North Wing renovation project commenced in September 2004.

County Libraries

Transfers to LibraryCo Inc. for county libraries operations were \$5.9 million, in line with 2003.

Repayable Allowance

In 2004, the Law Society's Repayable Allowance program provided \$285,000 to 85 students (2003: \$114,000 to 37 students).

Working Capital Reserve

The Working Capital Reserve of \$7.9 million is unchanged from 2003 and is funded in compliance with Convocation's policy.

Special Projects

The Fund expenses in 2004 were for the Sole Practitioner and Small Firm Task Force, significantly funded in the prior year. Most of the revenues were to fund the referendum on bench remuneration in 2005.

Auditors' Report

TO THE MEMBERS OF THE LAW SOCIETY OF UPPER CANADA,

We have audited the balance sheet of THE LAW SOCIETY OF UPPER CANADA – GENERAL FUND as at December 31, 2004 and the statements of revenues and expenses, changes in fund balances and cash flows for the year then ended. These financial statements are the responsibility of the Society's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the General Fund as at December 31, 2004 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

Chartered Accountants

Toronto, Ontario
February 11, 2005

General Fund

Balance Sheet

Stated in thousands of dollars

As at December 31

| | 2004 | 2003 |
|--|---------------|---------------|
| ASSETS | | |
| Current Assets | | |
| Cash and short-term investments | 22,222 | 26,245 |
| Accounts receivable (note 3) | 1,825 | 1,221 |
| Prepaid expenses | 155 | 309 |
| Total current assets | 24,202 | 27,775 |
| Portfolio investments (note 4) | 10,109 | — |
| Capital assets (note 5) | 18,121 | 16,965 |
| Total Assets | 52,432 | 44,740 |
| LIABILITIES AND FUND BALANCES | | |
| Current Liabilities | | |
| Accounts payable and accrued liabilities | 7,691 | 6,721 |
| Deferred revenue | 6,966 | 1,784 |
| Total current liabilities | 14,657 | 8,505 |
| Unclaimed trust funds (note 6) | 1,028 | 729 |
| Total Liabilities | 15,685 | 9,234 |
| FUND BALANCES | | |
| Unrestricted fund | 1,595 | — |
| Restricted funds | | |
| Capital allocation | 8,232 | 9,383 |
| Invested in capital assets | 18,121 | 16,965 |
| County libraries | 37 | 230 |
| Repayable allowance | 147 | 325 |
| Endowments | 466 | 498 |
| Special projects | 174 | 130 |
| Working capital reserve | 7,975 | 7,975 |
| Total Fund Balances | 36,747 | 35,506 |
| Total Liabilities and Fund Balances | 52,432 | 44,740 |

See accompanying notes

On behalf of Convocation



Treasurer



Chair of Finance and Audit Committee

Statement of Revenues and Expenses

Stated in thousands of dollars

Year ended December 31

| | 2004 | | | 2003 | | |
|---|----------------------|---------------------|---------------|----------------------|---------------------|---------------|
| | Unrestricted Fund | Restricted Funds | Total | Unrestricted Fund | Restricted Funds | Total |
| REVENUES | | | | | | |
| Membership fees | 27,252 | 7,884 | 35,136 | 26,348 | 7,540 | 33,888 |
| Professional development and competence | 12,160 | — | 12,160 | 11,253 | — | 11,253 |
| Investment income | 3,788 | 10 | 3,798 | 4,011 | 15 | 4,026 |
| Other (note 8) | 5,014 | 191 | 5,205 | 4,491 | 37 | 4,528 |
| Total revenues | 48,214 | 8,085 | 56,299 | 46,103 | 7,592 | 53,695 |
| EXPENSES | | | | | | |
| Professional development and competence | 17,018 | — | 17,018 | 14,551 | — | 14,551 |
| Professional regulation | 9,991 | — | 9,991 | 9,029 | — | 9,029 |
| Administrative | 6,419 | — | 6,419 | 6,233 | — | 6,233 |
| Other (note 9) | 5,096 | — | 5,096 | 4,997 | — | 4,997 |
| Client service centre | 3,933 | — | 3,933 | 3,516 | — | 3,516 |
| Facilities | 3,053 | — | 3,053 | 2,940 | — | 2,940 |
| Policy and legal affairs | 2,118 | — | 2,118 | 1,983 | — | 1,983 |
| Communications | 1,467 | — | 1,467 | 1,347 | — | 1,347 |
| Equity | 657 | — | 657 | 864 | — | 864 |
| Tribunals | 513 | — | 513 | 503 | — | 503 |
| Capital allocation fund | — | 615 | 615 | — | 815 | 815 |
| Invested in capital assets | | | | | | |
| — amortization | — | 1,613 | 1,613 | — | 1,485 | 1,485 |
| County libraries fund | — | 5,903 | 5,903 | — | 5,795 | 5,795 |
| Repayable allowance fund | — | 285 | 285 | — | 114 | 114 |
| Endowments | — | 42 | 42 | — | 12 | 12 |
| Special projects fund | — | 201 | 201 | — | 70 | 70 |
| Total expenses | 50,265 | 8,659 | 58,924 | 45,963 | 8,291 | 54,254 |
| Less: Expenses allocated to Lawyers Fund for Client Compensation (note 1) | 3,866 | — | 3,866 | 3,754 | — | 3,754 |
| Net expenses | 46,399 | 8,659 | 55,058 | 42,209 | 8,291 | 50,500 |
| Surplus (deficit) | 1,815 | (574) | 1,241 | 3,894 | (699) | 3,195 |

See accompanying notes

Statement of Changes in Fund Balances

Stated in thousands of dollars

Year ended December 31

2004

2003

RESTRICTED FUNDS

| | Unrestricted Fund | Capital Allocation | Invested in Capital Assets | County Libraries | Repayable Allowance | Endowments | Special Projects | Working Capital Reserve | Total Restricted Funds | Total | Total |
|---|----------------------|-----------------------|----------------------------------|---------------------|------------------------|-------------|---------------------|-------------------------------|------------------------------|---------------|---------------|
| Fund balances, beginning of year | — | 9,383 | 16,965 | 230 | 325 | 498 | 130 | 7,975 | 35,506 | 35,506 | 32,311 |
| Revenues | 48,214 | 2,233 | — | 5,710 | 7 | 10 | 125 | — | 8,085 | 56,299 | 53,695 |
| Expenses | 46,399 | 615 | 1,613 | 5,903 | 285 | 42 | 201 | — | 8,659 | 55,058 | 50,500 |
| Surplus (Deficit) | 1,815 | 1,618 | (1,613) | (193) | (278) | (32) | (76) | — | (574) | 1,241 | 3,195 |
| Interfund transfers | | | | | | | | | | | |
| Asset capitalization | — | (2,769) | 2,769 | — | — | — | — | — | — | — | — |
| Transfer to special projects | (120) | — | — | — | — | — | 120 | — | 120 | — | — |
| Transfer to repayable allowances | (100) | — | — | — | 100 | — | — | — | 100 | — | — |
| Total interfund transfers | (220) | (2,769) | 2,769 | — | 100 | — | 120 | — | 220 | — | — |
| Fund balances, end of year | 1,595 | 8,232 | 18,121 | 37 | 147 | 466 | 174 | 7,975 | 35,152 | 36,747 | 35,506 |

See accompanying notes

Statement of Cash Flows

Stated in thousands of dollars

Year ended December 31

| | 2004 | 2003 |
|---|-----------------|----------------|
| OPERATING ACTIVITIES | | |
| General fund surplus | 1,241 | 3,195 |
| Item not affecting cash: | | |
| Amortization of capital assets | 1,613 | 1,485 |
| Other operating sources (uses) of cash: | | |
| Accounts receivable | (604) | 731 |
| Prepaid expenses | 154 | (136) |
| Accounts payable and accrued liabilities | 970 | (524) |
| Deferred revenue | 5,182 | (2,623) |
| Fund contribution – unclaimed trusts | 299 | 294 |
| Total operating activities | 8,855 | 2,422 |
| INVESTING ACTIVITY | | |
| Portfolio investments (net) | (10,109) | – |
| Capital asset additions | (2,769) | (1,105) |
| Total investing activities | (12,878) | (1,105) |
| Net (decrease)/increase in cash and short-term investments | | |
| during the year | (4,023) | 1,317 |
| Cash and short-term investments, beginning of year | 26,245 | 24,928 |
| Cash and short-term investments, end of year | 22,222 | 26,245 |

See accompanying notes

Notes to Financial Statements

*Stated in whole dollars except where indicated
For the year ended December 31, 2004*

1. Description of Fund

The Law Society of Upper Canada (the "Society") was founded in 1797 and was incorporated in 1822 with the enactment of the *Law Society Act*. The Society exists to govern the legal profession in the public interest. This is achieved by ensuring that the people of Ontario are served by lawyers who meet high standards of learning, competence and professional conduct and by upholding the independence, integrity and honour of the legal profession, for the purpose of advancing the cause of justice and the rule of law. Convocation, the governing body of the Society, carries out this mandate.

The Society is not subject to income or capital taxes because it is a not-for-profit corporation. These financial statements represent the financial position and operations of the Law Society of Upper Canada – General Fund, which includes certain internally restricted funds, and do not purport to represent all assets and liabilities under the control of the Society.

Separate financial statements have been prepared for the following related entities, which have not been consolidated into the General Fund statements:

Lawyers Fund for Client Compensation

The Society maintains the Lawyers Fund for Client Compensation ("Compensation Fund") pursuant to section 51 of the *Law Society Act* to relieve or mitigate loss sustained by any person in consequence of dishonesty on the part of any member in connection with such member's law practice or in connection with any trust of which the member was or is a trustee. Members' annual fees and investment income finance the Compensation Fund. The Compensation Fund reports fees collected by the General Fund as revenues. The Compensation Fund reimburses the General Fund for certain administrative expenses, spot audit expense and a portion of the costs of operating the investigation and discipline functions of the Society. In 2004, these amounted to \$3,866,000 (2003- \$3,754,000).

Errors & Omissions Insurance Fund and Lawyers' Professional Indemnity Company

The Society provides professional liability insurance to the legal profession through the Errors and Omissions Insurance Fund ("E&O Fund") and the Lawyers' Professional Indemnity Company ("LAWPRO"). The E&O Fund was originally set up in the Society's accounts to record insurance claims and expenses and related levies and their investment. Prior to July 1, 1990 various insurance carriers underwrote the Errors and Omissions Insurance program. LAWPRO took over underwriting the program commencing July 1, 1990. LAWPRO, a wholly owned subsidiary of the Society, was incorporated in 1990 and is licensed to provide lawyer's professional liability and title insurance. On an annual basis the E&O Fund provides the General Fund with income derived from its surplus earnings. This income, reported as Investment Income of the General Fund, amounted in 2004 to \$3,000,000 (2003 – \$3,000,000). LAWPRO provided financial support in the amount of \$75,000 (2003 – \$0) for the Society's study on the future of small firms and sole practitioners. This funding is reported in the Special Projects Fund.

LibraryCo Inc.

LibraryCo Inc., a wholly owned, not-for-profit subsidiary of the Society, was established to develop policies, procedures, guidelines and standards for the delivery of county law library services across Ontario and to administer funding on behalf of the Society. LibraryCo Inc. was incorporated under the *Business Corporations Act of Ontario* in 2001. The Corporation issued 100 voting Common Shares to the Society for \$100 and 100 Special Shares to the County and District Law President's Association for \$100. The holders of the Special Shares are entitled to elect one director.

The Society levies and collects funds for County and District Law Library purposes and transfers these funds to LibraryCo. Convocation internally restricts these funds for use by county law libraries to carry out their annual operations and any special projects approved by Convocation.

Law Society Foundation

The Law Society Foundation ("LSF"), a registered charity, was incorporated by Letters Patent in October 1962. The objects of the LSF are to foster, encourage and promote legal education in Ontario, provide financial assistance to law students in Ontario, restore and preserve land and buildings of historical significance to Canada's legal heritage, receive gifts of muniments and legal memorabilia of interest and significance to Canada's legal heritage, to maintain a collection of gifts of books and other written material for use by educational institutions in Canada and to receive donations, and maintain a fund for the relief of poverty by providing meals to persons in need. The Society provides facilities, administration, accounting, security and certain other services at no cost to the LSF.

The Law Foundation of Ontario

The Law Foundation of Ontario ("LFO"), a corporation without share capital established in 1974, was created to receive interest accruing on monies held in lawyers' mixed trust accounts and to establish and maintain a fund to be used for the purposes of legal education and legal research, legal aid and the establishment, maintenance and operation of law libraries. During 2004, the LFO contributed to the General Fund of the Society \$1,300,000 (2003 – \$1,023,400) for the operation of the Bar Admission Course, \$100,000 (2003 – \$100,000) for legal heritage programs and \$29,000 (2003 – \$127,000) to support an access to justice symposium.

2. Significant Accounting Policies

Basis of presentation

The financial statements have been prepared in accordance with the accounting standards for not-for-profit organizations published by the Canadian Institute of Chartered Accountants using the restricted fund method of reporting revenues.

Description of funds

The *Unrestricted Fund* accounts for the Society's program delivery and administrative activities. This fund reports unrestricted resources.

Restricted Funds

The *Capital Allocation Fund* is maintained to provide a source of funds for the acquisition and maintenance of the Society's capital assets. These include buildings and major equipment including computers. Amounts of assets capitalized, according to the Society's Capital Asset policy, are transferred to the Invested in Capital Assets Fund. Expenditures not capitalized are expended in the Capital Allocation Fund. As at December 31, 2004 the balance is \$8,232,000 (2003 – \$9,383,000).

General Fund

The *Invested in Capital Assets Fund* records transactions related to the Society's capital assets, specifically acquisitions, amortization and disposals. As at December 31, 2004 the balance is \$18,121,000 (2003 – \$16,965,000)

The *County Libraries Fund* records transactions related to the Society's support of county law libraries. The fund accumulates levies raised by the Society for county library purposes. The Society remits amounts to LibraryCo Inc. on a predetermined basis as approved by Convocation. Amounts collected that exceed the current year requirement are held by the Society in the fund balance. This fund balance is available to reduce the amount levied on the membership in future years. At December 31, 2004 the fund balance was \$37,000 (2003 – \$230,000).

The *Repayable Allowance Fund* provides students with funding for tuition and living expenses and is based on a student's ability to repay the grant within a specified period of time following the student's non-participation in the Bar Admission Course. At December 31, 2004, the Fund Balance was \$147,000 (2003 – \$325,000).

The Society administers two *Endowment Funds*, the Law Society Trust and the J. Shirley Denison Fund. The Law Society Trust was established in accordance with the terms of the endowments so that the Society can award prizes, bursaries and gifts to deserving students in the Bar Admission Course. The J. Shirley Denison Fund was established to provide relief and assistance to members and former members who find themselves in difficult financial circumstances. Contributions for endowments are recognized as revenue in the Endowment Funds. For 2004, no funds were contributed for endowment purposes. At December 31, 2004, the Fund Balances totalled \$466,000 (2003 – \$498,000).

The *Special Projects Fund* is maintained to ensure that financing is available for ongoing special projects. The balance in the Special Projects Fund at December 31, 2004 is \$174,000 (2003 – \$130,000) primarily to fund the referendum on benchler remuneration.

The *Working Capital Reserve* is maintained to ensure adequate cash reserves for the continuous financing of the Society's operations. The balance is sufficient to provide for the Society's operating expenses for up to two months. As at December 31, 2004 the balance is \$7,975,000 (2003 – \$7,975,000).

Cash and short-term investments

Cash and short-term investments are amounts on deposit and invested in short-term (less than one year) investment vehicles according to the Society's investment policy and are subject to insignificant risk of a change in value. Investment income, except income earned on resources held for endowment, is retained in and reported by the Unrestricted Fund.

Capital assets

Assets are capitalized and subject to amortization when they are determined to have a minimum useful life of three years and an acquisition cost of \$10,000 for equipment, furniture and computer equipment, \$25,000 for computer software and \$25,000 for building improvements. Capital Assets are presented at cost net of accumulated amortization and grants. For purposes of calculating the first year's amortization, all capital assets are deemed to be acquired, put into service, or completed on July 1st. Amortization is charged to expense on a straight-line basis over the estimated useful lives of the assets as follows:

| | |
|---|--------------|
| Buildings | 30 years |
| Building improvements | 10 years |
| Furniture, equipment and computer hardware and software | 3 to 5 years |

Revenue recognition

Membership fees are recognized in the year to which they relate if the amount can be reasonably estimated and collection is reasonably assured. Accordingly, fees for the next fiscal year received prior to December 31 have been deferred and are recognized as revenue in the next calendar year.

Professional Development and Competence, investment and other revenues are recognized when receivable if the amount can be reasonably estimated and collection is reasonably assured.

Collections

The Society owns a collection of legal research and reference material as well as a collection of portraits and sculptures. The cost of additions to the collections is expensed as incurred. No value is recorded in these financial statements for donated items.

Volunteer services

The work of the Society is dependent on the voluntary services of the elected Benchers and other members of the profession. These services are received gratuitously; therefore, no value has been included in these financial statements.

Financial instruments

The estimated fair values of cash and short-term investments, accounts receivable, prepaid expenses, accounts payable, accrued liabilities and deferred revenue approximate their carrying amounts in the financial statements due to the relatively short period to maturity of these instruments.

Measurement uncertainty

The preparation of the financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingencies at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

3. Accounts Receivable

Included in accounts receivable are certain amounts receivable from related parties as follows:

| | 2004 | 2003 |
|---|---------|---------|
| Lawyers Fund for Client Compensation | 277,673 | 164,620 |
| LibraryCo Inc. | – | 7,680 |
| The Law Society Foundation | – | 11,541 |
| The Law Foundation of Ontario | 389,781 | 320,607 |
| Lawyers' Professional Indemnity Company | 93,047 | 21,223 |

General Fund

4. Portfolio Investments

| (\$000's) | 2004 | | 2003 |
|-----------------|------------|--------------|-----------------------|
| | Book Value | Market Value | Book and Market Value |
| Debt Securities | 8,335 | 8,233 | – |
| Common Shares | 1,774 | 1,755 | – |
| | 10,109 | 9,988 | – |

5. Capital Assets

| (\$000's) | 2004 | | | 2003 |
|---|--------|--------------------------|--------|--------|
| | Cost | Accumulated Amortization | Net | Net |
| Land and buildings | 27,947 | 16,654 | 11,293 | 11,883 |
| Building improvements | 7,247 | 2,520 | 4,727 | 3,932 |
| Building improvements under construction | 1,289 | – | 1,289 | 136 |
| Furniture, equipment and computer hardware and software | 3,447 | 2,635 | 812 | 1,014 |
| | 39,930 | 21,809 | 18,121 | 16,965 |

In 2004 construction commenced on the renovation of Osgoode Hall's North Wing. Renovations are expected to be completed in 2006 at a total cost of \$9,028,000, funded from balances accumulated in the Capital Allocation Fund. Expenditures relating to this renovation, categorized as building improvements under construction, total \$1,289,000. These assets will not be depreciated until the renovation is complete.

6. Unclaimed Trust Funds

Section 59.6 of the *Law Society Act* permits a member who has held money in trust for or on account of a person for a period of at least two years to apply in accordance with the by-laws for permission to pay the money to the Society. Money paid to the Society is held in trust in perpetuity for the purpose of satisfying the claims of the persons who are entitled to the capital amount. Subject to certain provisions in the Act which enable the Society to recover its expenses associated with maintaining these funds, all net income from the money held in trust shall be paid to the Law Foundation of Ontario. Unclaimed money held in trust amounts to \$1,028,000 (2003 – \$729,000).

7. Other Trust Funds

The Society administers client funds for members under voluntary or court-ordered trusteeships. These funds and matching liabilities are not reflected on the balance sheet. Money paid to the Society is held in trust until it is repaid to the clients or transferred to the Unclaimed Trust Funds. At December 31, 2004 total funds held in trust amounted to \$2,286,000 (2003 – \$1,293,000).

8. Other Revenue

Included in other revenue is income from the *Ontario Reports*, catering, the Lawyer Referral Service, specialist certification and other miscellaneous revenues.

9. Other Expenses

Included in other expenses are payments to the Federation of Law Societies, County and District Law Presidents' Association, insurance, professional fees, governance related disbursements, termination payments, catering and other corporate expenses.

10. Pension Plan

The Society maintains a defined contribution plan for all eligible employees of the Society. In prior years, matching employee and employer contributions each ranged from a minimum of 4.5% to a maximum of 6% of earnings. From the beginning of 2004, Law Society employees could choose matching employee and employer contributions between 1% and 6% of earnings. The Society's pension expense in 2004 amounted to \$1,180,000 (2003 – \$943,000).

11. Commitments

The Society is committed to monthly lease payments for property and equipment under leases having various terms up to the end of April 2010. Aggregate minimum monthly payments over the next years are as follows:

| Year | \$000's |
|-------|---------|
| 2005 | 345 |
| 2006 | 364 |
| 2007 | 377 |
| 2008 | 399 |
| 2009 | 410 |
| 2010 | 138 |
| Total | 2,033 |

At December 31, 2004 contractual obligations relating to the renovation of Osgoode Hall's North Wing totalled \$5,223,000 (2003 – nil).

12. Contingent Liabilities

A number of claims or potential claims are pending against the Society. It is not possible for the Society to predict with any certainty the outcomes of such claims or potential claims. Management is of the opinion that based on the information presently available, it is unlikely that any liability, to the extent not covered by insurance, would be material to the Society's financial position.

13. Guarantees

In the normal course of business the Society has entered into agreements that meet the definition of a guarantee, including indemnities in favour of third parties, such as confidentiality agreements, engagement letters with advisors and consultants, outsourcing agreements, leasing contracts, information technology agreements and service agreements. Under the terms of these agreements, the Society agrees to indemnify the counterparties for various items including, but not limited to, all liabilities, loss, suits, and damages arising during, on or after the term of the agreement. The maximum amount of any potential future payment cannot be reasonably estimated.

The Society has also provided indemnification to all directors and officers of the Society. Under section 9 of the *Law Society Act*:

"No action or other proceedings for damages shall be instituted against the Treasurer or any benchers, official of the Society or person appointed in Convocation for any act done in good faith in the performance or intended performance of any duty or in the exercise or in the intended exercise of any power under this Act, a regulation, a by-law or a rule of practice and procedure, or for any neglect or default in the performance or exercise in good faith of any such duty or power."

Notwithstanding section 9, the Society has also purchased errors and omissions insurance for past and present officers, employees, committee members, benchers, agents and volunteers acting on behalf of the Society, its subsidiaries and affiliates, to mitigate the cost of any potential suit or action.

No estimate of the maximum exposure under these indemnifications can be made and historically the Society has not made any significant payments under such or similar indemnification agreements. Therefore no amount has been accrued in the financial statements with respect to these agreements.

14. Comparative Figures

Certain of the prior year's comparative figures have been reclassified to conform to the current year's financial statement presentation.

Management Discussion and Analysis

The Lawyers Fund for Client Compensation is maintained by the Law Society, in accordance with the *Law Society Act*, to relieve or mitigate loss sustained by any person in consequence of dishonesty on the part of any member in connection with such member's law practice or in connection with any trust of which the member was or is a trustee. The Fund is financed by members' annual fees and investment income.

The Compensation Fund has enjoyed a fourth consecutive year of moderate claims against the Fund. This has contributed to an increase of \$2.1 million in the Fund's year-end balance from \$17.4 million to \$19.5 million.

BALANCE SHEET

Cash and short-term investments

The Compensation Fund's short-term investments are invested in bankers' acceptances, Government of Canada T-bills and cash.

Portfolio investments

Portfolio, or long-term investments (\$21.2 million compared to \$19.8 million in 2003) are comprised of 82% fixed income and 18% North American equities. Fixed income investments comprise a diversified mix of government, provincial and corporate bonds with an investment rating of "BBB" or better. Equity investments comprise a diversified mix of equities listed on the New York and Toronto stock exchanges. The market value of the portfolio is \$21.7 million.

Reserve for unpaid grants

Based upon the actuarial valuation of the grant reserve, the reserve for unpaid grants has decreased by \$800,000 to \$9.0 million.

STATEMENT OF REVENUES AND EXPENSES AND CHANGE IN FUND BALANCE

Revenues

Membership fees

The Compensation Fund's claim experience in recent years has permitted a decrease in membership fees declining from \$280 per member in 2003 to \$230 per member in 2004. This decrease was partially offset by approximately 700 more members in 2004, leading to the decrease in total membership fees from \$7.8 million to \$6.7 million.

Investment income

Investment income has increased to \$1.5 million in 2004 from \$1.3 million in 2003 as a result of a higher rate of return on the long-term portfolio that included net realized gains of \$542,000. Total return on all the Fund's investments was 5.2% in 2004 compared to 4.2% in 2003.

Expenses

Grants

Along with the favourable movement in the actuarial reserve, grants paid during the year decreased from \$2.7 million in 2003 to \$2 million in line with grant trends over recent years.

Insurance

Insurance premiums of \$495,000 and coverage was unchanged between 2003 and 2004.

Other expenses

The Compensation Fund's 2004 operating expenses were generally stable compared to 2003.

Lawyers Fund for Client Compensation

Auditors' Report

TO THE MEMBERS OF THE LAW SOCIETY OF UPPER CANADA,

We have audited the balance sheet of THE LAW SOCIETY OF UPPER CANADA – LAWYERS FUND FOR CLIENT COMPENSATION as at December 31, 2004 and the statements of revenues and expenses and change in fund balance and of cash flows for the year then ended. These financial statements are the responsibility of the Society's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Fund as at December 31, 2004 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

Chartered Accountants

Toronto, Ontario

February 11, 2005

Lawyers Fund for Client Compensation



Balance Sheet

Stated in thousands of dollars
As at December 31

| | 2004 | 2003 |
|---|---------------|---------------|
| ASSETS | | |
| Current Assets | | |
| Cash and short-term investments | 7,688 | 8,222 |
| Interest and other receivables | 117 | 166 |
| Total Current Assets | 7,805 | 8,388 |
| Portfolio investments (note 4) | 21,234 | 19,829 |
| Total Assets | 29,039 | 28,217 |
| LIABILITIES AND FUND BALANCE | | |
| Accounts payable and accrued liabilities (note 5) | 468 | 926 |
| Reserve for unpaid grants | 9,040 | 9,854 |
| Total Liabilities | 9,508 | 10,780 |
| Fund Balance | 19,531 | 17,437 |
| Total Liabilities and Fund Balance | 29,039 | 28,217 |

See accompanying notes

On behalf of Convocation

Treasurer

Chair of Finance and Audit Committee

Lawyers Fund for Client Compensation

Statement of Revenues and Expenses and Change in Fund Balance

Stated in thousands of dollars

Year ended December 31

| | 2004 | 2003 |
|---------------------------------------|---------------|---------------|
| REVENUES | | |
| Membership fees | 6,667 | 7,857 |
| Investment income | 1,485 | 1,287 |
| Total revenues | 8,152 | 9,144 |
| EXPENSES | | |
| Grants paid | 2,010 | 2,701 |
| Decrease in reserve for unpaid grants | (814) | (827) |
| Recoveries | (87) | (165) |
| Net grants expense | 1,109 | 1,709 |
| Spot audit | 1,987 | 1,838 |
| Share of investigation and discipline | 987 | 1,046 |
| Administrative | 1,052 | 1,035 |
| Insurance | 495 | 495 |
| Salaries and benefits | 428 | 512 |
| Total expenses | 6,058 | 6,635 |
| Surplus | 2,094 | 2,509 |
| Fund balance, beginning of year | 17,437 | 14,928 |
| Fund balance, end of year | 19,531 | 17,437 |

See accompanying notes

Statement of Cash Flows

Stated in thousands of dollars

Year ended December 31

| | 2004 | 2003 |
|--|--------------|----------------|
| OPERATING ACTIVITIES | | |
| Surplus | 2,094 | 2,509 |
| Items not affecting cash: | | |
| Decrease in reserve for unpaid grants | (814) | (827) |
| Other operating sources (uses) of cash: | | |
| Interest and other receivables | 49 | (16) |
| Accounts payable and accrued liabilities | (458) | 182 |
| Total operating activities | 871 | 1,848 |
| FINANCING ACTIVITY | | |
| Portfolio investments (net) | (1,405) | (5,856) |
| Net decrease in cash and short-term investments during the year | (534) | (4,008) |
| Cash and short-term investments, beginning of year | 8,222 | 12,230 |
| Cash and short-term investments, end of year | 7,688 | 8,222 |

See accompanying notes

Lawyers Fund for Client Compensation

Notes to Financial Statements

Stated in whole dollars except where indicated

For the year ended December 31, 2004

1. Description of Fund

The Lawyers Fund for Client Compensation (the "Fund") is maintained by The Law Society of Upper Canada (the "Society") pursuant to section 51 of the *Law Society Act* to relieve or mitigate loss sustained by any person in consequence of dishonesty on the part of any member in connection with such member's law practice or in connection with any trust of which the member was or is a trustee. The Fund is financed by members' annual fees and investment income.

The Fund is not subject to income or capital taxes because it is a fund of the Society, a not-for-profit corporation.

The Fund reimburses the Society's General Fund for certain administrative expenses, spot audit expenses and a portion of the costs of operating the investigation and discipline functions of the Society. The charges for the year amount to \$3,866,000 (2003 – \$3,754,000).

2. Significant Accounting Policies

Basis of presentation

The financial statements have been prepared in accordance with the accounting standards for not-for-profit organizations published by the Canadian Institute of Chartered Accountants, using the restricted fund method of reporting revenues. The Fund accounts for the program delivery, administration and payment of grants from the Fund. The Fund is restricted in use by the *Law Society Act*.

Cash and short-term investments

Cash and short-term investments are amounts on deposit and invested in short-term (less than one year) investment vehicles according to the Society's investment policy and are subject to an insignificant risk of change in value.

Portfolio investments

Portfolio investments are recorded at cost, net of amortization of premiums and discounts. Investments consist of a diversified portfolio of government bonds, corporate bonds and Canadian and U.S. equities, according to the Society's investment policy. Only if a loss in the value of an investment is other than a temporary decline is the investment written down to recognize the loss.

Revenue recognition

Membership fees are recognized in the year to which they relate if the amount can be reasonably estimated and collection is reasonably assured. Investment income is recognized when receivable if the amount can be reasonably estimated.

Grants

Pursuant to section 51(5) of the *Law Society Act*, the payment of grants from the Fund is at the discretion of Convocation. Grants paid are subject to a \$100,000 limit per applicant. A reserve for unpaid grants is recorded as a liability on the balance sheet. This reserve represents an estimate of the present value of grants to be paid for unprocessed claims and the associated administrative costs, as determined by an actuary. The related net grants

expense represents grant payments during the year plus the current year experience gain/loss of the reserve for unpaid grants, net of recoveries. In 2004, the Fund maintained insurance for cumulative claims in excess of \$15,000,000 to a maximum of \$25,000,000. This insurance has been discontinued for the 2005 year.

Financial instruments

The estimated fair values of cash and short-term investments, interest and other receivables and accounts payable and accrued liabilities approximate their carrying amounts in the financial statements due to the relatively short period to maturity of these instruments.

3. Measurement Uncertainty

The valuation of unpaid grants anticipates the combined outcomes of events that are yet to occur. There is uncertainty inherent in any such estimations and therefore a limitation upon the accuracy of these valuations. Future loss emergence may deviate from these estimates. No provision has been made for otherwise unforeseen changes to the legal or economic environment in which claims are settled, nor for causes of loss which are not already reflected in the historical data. Management believes that the techniques employed and assumptions made are appropriate and the conclusions reached are reasonable given the information currently available. Estimates of unpaid grants are reviewed at least annually by an actuary and, as adjustments become necessary, they are reflected in current operations.

4. Portfolio Investments

As at December 31

| (\$000's) | 2004 | | 2003 | |
|-----------------|---------------|---------------|---------------|---------------|
| | Book Value | Market Value | Book Value | Market Value |
| Debt Securities | 17,587 | 17,788 | 16,908 | 17,191 |
| Common Shares | 3,647 | 3,904 | 2,921 | 3,171 |
| | 21,234 | 21,692 | 19,829 | 20,362 |

5. Accounts Payable and Accrued Liabilities

Included in accounts payable and accrued liabilities is an amount due to the Society's General Fund of \$277,673 (2003 – \$164,620).

6. Comparative Figures

Certain of the prior year's comparative figures have been reclassified to conform to the current year's financial statement presentation.

Errors and Omissions Insurance Fund

Management Discussion and Analysis

COMBINED BALANCE SHEET

Investments

Investment assets, inclusive of cash and cash equivalents, increased by \$34.2 million to \$363.2 million at December 31, 2004. These additional funds represent funds held to offset increased claims obligations plus surplus funds generated in the year. Investment assets are managed in accordance with investment policy in a diversified, high quality portfolio of fixed income (88%) and equity (12%) products.

Provision for unpaid claims and adjustment expenses and reinsurers' share of provision

The reinsurers' share of the provision for unpaid claims and adjustment expenses decreased from \$110.9 million in 2003 to \$97.7 million in 2004. The decline is due to the continued transitional effects of ceding lesser portions of the Ontario professional liability program. The percentage ceded dropped in stages from 57% in 1995 to nil in 2003 where it remained in 2004. The provision for unpaid claims, which represents the amount required to satisfy all obligations to claimants without offset for reinsurance, has increased from \$311.8 million in 2003 to \$321.8 million in 2004.

Surplus

The surplus has increased by \$10.8 million, the excess of revenue over expenses for the year.

COMBINED STATEMENT OF REVENUE AND EXPENSES

In 2004, the Errors and Omissions Insurance Fund generated an excess of revenue over expenses of \$10.8 million, a decrease of \$2.0 million from 2003. Total expenses increased by \$0.7 million in 2004 to \$91.2 million and revenues decreased by \$1.3 million to \$101.9 million.

Members' levies

Members' levies decreased by \$9.1 million in 2004 to \$68.1 million. While the base annual levy for the Ontario professional liability program remained consistent at \$2,500 in 2004, no premium subsidies were drawn from the premium stabilization fund in 2004, compared with \$6.1 million in 2003.

Other insurance premiums

Other insurance premiums increased to \$11.3 million from \$9.3 million in 2003 as a result of growth in title and excess professional liability insurance.

Investment income

The Combined Fund generated \$19.8 million of investment income, an increase of \$6.1 million from the prior year, which includes net capital gains of \$5.1 million (2003 – \$0.8 million) realized on the disposition of assets. Typically, over 85% of the investment portfolio consists of debt securities. At year-end, the market value of the portfolio exceeded book value by almost \$13.1 million (2003 – \$10.0 million).

Net claims and adjustment expenses

Overall, incurred claims are consistent with the prior year. An improvement in prior year loss estimates in the amount of \$8.0 million offset an increase in the number of claims reported in 2004.

Reinsurance premiums

The increase in costs of reinsurance is primarily due to higher premiums generated by the excess professional liability program, which is fully reinsured.

General expenses

The increase in general expenses of \$1.2 million from 2003 levels is primarily attributable to increased compensation and benefits related costs.

Errors and Omissions Insurance Fund

Auditors' Report

TO THE MEMBERS OF THE LAW SOCIETY OF UPPER CANADA

We have audited the combined balance sheet of THE LAW SOCIETY OF UPPER CANADA – ERRORS AND OMISSIONS INSURANCE FUND as at December 31, 2004 and the combined statements of revenue and expenses and surplus and of cash flows for the year then ended. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these combined financial statements present fairly, in all material respects, the financial position of the Fund as at December 31, 2004 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

Chartered Accountants

Toronto, Ontario

January 28, 2005

Actuary's Report

For Combined Financial Statements at December 31, 2004

ROLE OF THE VALUATION ACTUARY

The valuation actuary is appointed by the Audit Committee of the Lawyers' Professional Indemnity Company in its capacity as manager of the Law Society of Upper Canada Errors and Omissions Insurance Fund. With respect to the preparation of these combined financial statements, the actuary is required to carry out a valuation of the claims liabilities and to report thereon to the Audit Committee, and through it to the membership of the Law Society. The valuation is carried out in accordance with accepted actuarial practice, and regulatory requirements. The scope of the valuation encompasses the claims liabilities, that is the provision for unpaid claims and adjustment expenses on claims incurred and reported prior to December 31, 2004, the date of these combined financial statements.

In performing the valuation of the liabilities for these future events, which are by their very nature inherently variable, the actuary makes assumptions as to future rates of claims severity, inflation, reinsurance recoveries, expenses and other matters, taking into consideration the circumstances of the Errors and Omissions Insurance Fund, the Lawyers' Professional Indemnity Company and the nature of the insurance coverage being offered. The valuation is necessarily based on estimates, consequently, the final values may vary significantly from those estimates. The actuary also makes use of management information provided by the Law Society and the Lawyers' Professional Indemnity Company, and uses the work of the auditor with respect to the verification of the underlying data used in the valuation.

VALUATION ACTUARY'S REPORT

I have valued the claims liabilities arising on the errors and omissions insurance coverage arranged by the Law Society of Upper Canada for its Errors and Omissions Insurance Fund combined balance sheet as at December 31, 2004, and their changes in its combined statement of revenue and expenses and surplus for the year then ended, in accordance with accepted actuarial practice, including selection of appropriate assumptions and methods.

In my opinion, the amount of the claims liabilities makes appropriate provision for all such obligations, and the financial statements fairly present the results of the valuation.



Brian G. Pelly
Fellow, Canadian Institute of Actuaries

Toronto, Ontario
January 28, 2005

Errors and Omissions Insurance Fund

Combined Balance Sheet

Stated in thousands of dollars

As at December 31

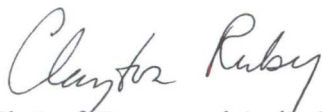
| | 2004 | 2003 |
|--|----------------|----------------|
| ASSETS | | |
| Cash and cash equivalents | 32,289 | 9,877 |
| Investments (note 4) | 330,942 | 319,186 |
| Investment income due and accrued | 2,287 | 2,539 |
| Accounts receivable | 12,959 | 12,570 |
| Reinsurers' share of provision for unpaid claims and adjustment expenses (note 6) | 97,663 | 110,866 |
| Other receivables | 928 | 1,292 |
| Other assets | 386 | 320 |
| Fixed assets (accumulated depreciation 2004 – 5,582; 2003 – 4,898) | 729 | 1,076 |
| Income tax recoverable | 3,224 | – |
| Future income taxes | 5,495 | 4,230 |
| Total assets | 486,902 | 461,956 |
| LIABILITIES AND SURPLUS | | |
| Provision for unpaid claims and adjustment expenses (notes 3 and 6) | 321,799 | 311,788 |
| Premium stabilization fund (note 8) | 25,502 | 20,431 |
| Accounts payable and accrued liabilities | 5,797 | 6,684 |
| Surplus (note 5) | 133,804 | 123,053 |
| Total liabilities and surplus | 486,902 | 461,956 |

See accompanying notes

On behalf of Convocation:



Treasurer



Chair of Finance and Audit Committee

Combined Statement of Revenue and Expenses and Surplus

Stated in thousands of dollars

Year ended December 31

| | 2004 | 2003 |
|---|----------------|----------------|
| REVENUE | | |
| Members' levies, mandatory insurance program (<i>notes 7 and 8</i>) | 68,071 | 77,123 |
| Other insurance premiums | 11,271 | 9,313 |
| Reinsurance commissions | 2,803 | 3,073 |
| Investment income | 19,758 | 13,691 |
| Total revenue | 101,903 | 103,200 |
| EXPENSES | | |
| Net claims and adjustment expenses (<i>notes 3 and 6</i>) | 64,532 | 65,142 |
| Reinsurance premiums | 5,304 | 4,527 |
| General expenses | 12,945 | 11,708 |
| Transfer to Law Society General Fund (<i>note 9</i>) | 3,000 | 3,000 |
| Premium taxes | 2,405 | 2,619 |
| Provision for income taxes | 2,966 | 3,426 |
| Total expenses | 91,152 | 90,422 |
| Excess of revenue over expenses | 10,751 | 12,778 |
| Surplus, beginning of year | 123,053 | 110,275 |
| Surplus, end of year | 133,804 | 123,053 |

See accompanying notes

Errors and Omissions Insurance Fund

Combined Statement of Cash Flows

Stated in thousands of dollars

Year ended December 31

| | 2004 | 2003 |
|---|-----------|-----------|
| OPERATING ACTIVITIES | | |
| Excess of revenue over expenses | 10,751 | 12,778 |
| Items not affecting cash: | | |
| Depreciation | 684 | 695 |
| Future income taxes | (1,265) | (3,765) |
| Realized gains | (5,147) | (763) |
| Amortization of discount/(premiums) on bonds | 436 | (2,046) |
| | 5,459 | 6,899 |
| Other operating sources (uses) of cash: | | |
| Investment income due and accrued | 252 | 734 |
| Amounts receivable and other assets | (3,315) | 2,865 |
| Reinsurers' share of provision for unpaid claims and adjustment expenses | 13,203 | 22,216 |
| Provision for unpaid claims and adjustment expenses | 10,011 | 3,268 |
| Premium stabilization fund | 5,071 | (5,400) |
| Accounts payable and accrued liabilities | (887) | (5,813) |
| Total funds provided by operating activities | 29,794 | 24,769 |
| INVESTING ACTIVITIES | | |
| Fixed assets: | | |
| Purchase of fixed assets | (337) | (317) |
| Investments: | | |
| Purchases of investments | (280,355) | (872,532) |
| Proceeds from sale of investments | 273,310 | 855,171 |
| Investment purchases, net | (7,045) | (17,361) |
| Total funds provided by investing activities | (7,382) | (17,678) |
| Net change in cash and cash equivalents | 22,412 | 7,091 |
| Cash and cash equivalents, beginning of year | 9,877 | 2,786 |
| Cash and cash equivalents, end of year | 32,289 | 9,877 |
| Cash and cash equivalents at the end of year consist of: | | |
| Cash | 7,145 | 1,405 |
| Cash equivalents | 25,144 | 8,472 |

See accompanying notes

Notes to Combined Financial Statements

Stated in whole dollars except where indicated

As at December 31, 2004

1. The Insurance Program and its Risk Retention and Reinsurance Structure

The combined financial statements of the Errors and Omissions Insurance Fund ("the Combined Fund") account for the net results of the professional liability insurance program of the Law Society of Upper Canada ("the Society"). The program requires practising members to pay annual levies to fund the anticipated costs of professional liability claims made in each annual policy period. Indemnification of members is subject to the terms of the insurance policy, including financial limits per claim and aggregate limits per member in each policy period.

These financial statements combine the results of operations, financial positions and cash flows of:

- the Errors and Omissions Insurance Fund of the Society ("the Fund"), the fund originally set up in the Society's accounts to record insurance claims and expenses and related levies and their investments; and
- Lawyers' Professional Indemnity Company ("LAWPRO"), a wholly owned subsidiary of the Society that was incorporated in 1990 as an insurance company and is licensed to provide lawyers' professional liability and title insurance.

The risk retention and reinsurance structures employed through these two entities are described in the following paragraphs.

Prior to July 1, 1990, the Society's Errors and Omissions Insurance Program was underwritten by various insurance carriers subject to a policy deductible. LAWPRO took over the underwriting of the program commencing July 1, 1990. The Society maintained financial responsibility for the policy deductible through to December 31, 1994. The policy deductible was a combination of a group deductible and the individual member deductibles. For the periods noted below, the combined policy deductibles were as follows:

| | |
|-------------------------------|---------------------------|
| July 1989 to June 1990 | \$ 250,000 per occurrence |
| July 1990 to December 1991 | \$ 200,000 per occurrence |
| January 1992 to December 1994 | \$ 250,000 per occurrence |

The Society was not able to arrange Stop Loss reinsurance on its group deductible after the policy period ending June 1989. As a result, the full financial risk of the deductible rested with the Society, from July of 1989 through the policy period ended December 1994.

LAWPRO also had a net retention above the policy's group deductible as follows:

- July 1, 1990 to December 31, 1991: LAWPRO is liable for \$50,000 of all individual losses in excess of \$200,000;
- January 1, 1992 to December 31, 1992: LAWPRO is liable for an aggregate of \$2,500,000 from individual losses incurred in excess of \$250,000 plus a further 10% of all losses above \$250,000 once the initial \$2,500,000 limit has been reached; and
- January 1, 1993 to December 31, 1994: LAWPRO is liable in each policy year for an aggregate of \$4,000,000 if incurred losses are above or exceed \$250,000 plus a further 10% of all losses in excess of \$250,000 once the initial \$4,000,000 limit has been reached.

Errors and Omissions Insurance Fund

It was decided, effective January 1, 1995, to eliminate the self-insured group deductible. Commencing January 1, 1995, 100% of the risk over the individual member deductibles is insured within LAWPRO. LAWPRO in turn reinsures a portion of its risk retention with third party Canadian licensed reinsurers.

The policy limits for the period January 1, 2004 through December 31, 2004 are \$1 million per claim and \$2 million per member in aggregate.

2. Significant Accounting Policies

These combined financial statements have been prepared in accordance with Canadian generally accepted accounting principles. The most significant accounting policies are as follows:

Members' Levies, Mandatory Insurance Program and Other Insurance Premiums

Members' levies are recorded when billed with the exception of those based on transactions. The transaction levy, first introduced in 1995, is recorded on a cash basis based on members' filings.

Other Insurance Premiums represent revenues generated from non-mandatory programs including title insurance and excess professional liability coverage. These transactions are recorded as revenue at the inception date of policies.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, balances with banks, and short-term investments with maturities of three months or less. The fair value of cash and cash equivalents approximates the amounts shown in the financial statements.

Investments

Investments in debt securities are recorded at amortized cost. Premiums and discounts from par value are amortized on a straight-line basis over the term to maturity. Investments in common or preferred shares are carried at cost. Gains and losses on investments are included in investment income when realized. Any losses in value of an investment, which are considered other than temporary in nature, are recognized in income.

Fixed assets

Fixed assets are presented at cost, net of accumulated depreciation and amortization. Depreciation and amortization are charged to expense on a straight-line basis over the estimated useful lives of the assets as follows:

| | |
|-------------------------|---------------|
| Leasehold improvements | Term of lease |
| Furniture and equipment | 3 to 5 years |
| Software | 1 to 3 years |

Claims related balances

a) Provision for unpaid claims and adjustment expenses

The insurance program covers claims made against insureds in the policy period.

The provision is determined using case-basis evaluations plus an amount for future development and delayed reporting and is an estimation of the ultimate discounted cost of all insurance claims to December 31, 2004. The estimates are regularly reviewed and updated and any resulting adjustments are included in current income.

The provision for unpaid claims is presented net of a discount that reflects an estimation of the investment income that will be earned on funds until they are paid out in settlement of claims. Accordingly, the provision as recorded represents fair value. The estimation of the discount is based on anticipated investment rates of return and experience with payout patterns on similar types of claims.

b) Reinsurers' share of provisions for unpaid claims and adjustment expenses

Expected reinsurance recoveries on unpaid claims and adjustment expenses are recognized as assets at the same time as, and using principles consistent with, the Society's method for establishing the related liability.

c) Members' deductibles

The insurance policy calls for insured members to pay deductibles, which range from nil up to \$25,000. Expected deductible recoveries on paid and unpaid claims are recognized net of any required provision for uncollectible accounts, using principles consistent with the Combined Fund's method for establishing the related claims liability.

Employee future benefits

LAWPRO maintains a defined contribution plan for its employees as well as a supplemental defined benefit plan for certain designated employees which provides benefits to those employees in excess of the benefits provided by the Company pension plan. The cost of the supplemental defined benefit plan is actuarially determined using the projected benefit method pro-rated on service and management's best estimate of the expected plan investment performance, salary escalation and retirement ages of employees. Market values are used to value benefit plan assets. The obligation related to employee future benefits is measured using current market interest rates assuming a portfolio of corporate long bonds with terms to maturity in accordance with the requirements of the Canadian Institute of Chartered Accountants ("CICA") standard, "Employee Future Benefits."

Adjustments for plan amendments, changes in assumptions and actuarial gain and losses are charged fully into income in the year they are realized.

Income taxes

LAWPRO uses the asset and liability method of accounting for income tax purposes. Under the asset and liability method of tax allocation, future income tax assets and liabilities are determined based on the differences between the financial reporting and tax basis of assets and liabilities, and are measured using the substantively enacted tax rates and laws that are expected to be in effect in the periods in which the future income tax assets or liabilities are expected to be settled or realized.

The Fund is not subject to income or capital taxes because it is a not-for-profit corporation.

3. Measurement Uncertainty

The settlement of professional liability claims involves processes, the outcome of which is inherently uncertain. Consequently, the estimation of the ultimate settlement costs of claims made to date, that underlies the provision for unpaid claims and adjustment expenses, involves measurement uncertainty. The amounts are necessarily based on estimates of future trends in claim severity and other factors, which could vary as the claims are settled. Ultimate costs incurred will inevitably vary from current estimates, to some extent. Although it is not possible to measure the degree of variability inherent in such estimates, management believes that the provision for unpaid claims and adjustment expenses is adequate. Estimates are reviewed at least annually by an actuary and, as adjustments to these liabilities become necessary, they are reflected in current operations.

There is also measurement uncertainty inherent in the estimation of reinsurance recoveries and members' deductible recoveries. Management is satisfied that appropriate provisions have been made for potentially unrecoverable amounts and believes that any remaining exposure would prove immaterial to these financial statements.

Errors and Omissions Insurance Fund

4. Investment Information

The Fund and LAWPRO hold a diversified portfolio consisting of equities and fixed income securities with investment grades of "A" or better.

Estimated fair values

The book values and estimated fair values of investments as at December 31 were as follows:

| (000's) | 2004 | | | 2003 | | |
|------------------|------------|----------------------|---------|------------|----------------------|---------|
| | Book value | Estimated fair value | Yield % | Book value | Estimated fair value | Yield % |
| Debt Securities | 292,211 | 298,772 | 4.5 | 285,790 | 290,690 | 4.3 |
| Common Shares | 36,132 | 42,524 | | 28,540 | 33,448 | |
| Preferred Shares | 2,599 | 2,753 | | 4,856 | 5,035 | |
| | 330,942 | 344,049 | | 319,186 | 329,173 | |

The estimated fair values of debt securities, common and preferred shares are based on quoted market values.

Liquidity and interest rate risk

The maturity profile of debt securities as at December 31, 2004 is as follows:

| (000's) | Within 1 year | 1 to 5 years | Over 5 years | Book value |
|-------------------|---------------|--------------|--------------|------------|
| Debt securities | 415 | 181,327 | 110,469 | 292,211 |
| Per cent of total | 0.1% | 62.1% | 37.8% | |

The average duration of debt securities at December 31, 2004 is 4.09 years. LAWPRO attempts to match the maturity of these investments to the expected maturity of claims obligations. Shares have no specific maturities.

5. Surplus

The Surplus of the Combined Fund includes LAWPRO's capital and surplus. At December 31, 2004 the capital and surplus of LAWPRO, as reported under insurance regulatory requirements, was \$102.2 million (2003 – \$96.2 million).

6. Claims and Adjustment Expenses

Reinsurance ceded

To limit losses through the spreading of risks, the Fund and LAWPRO cede reinsurance to other insurers. Net claims and adjustment expenses presented in the combined statement of revenue and expenses are net of reinsurance ceded in the amounts of \$7.0 million (2003 – \$3.0 million).

In the event that a reinsurer is unable to meet obligations assumed under reinsurance agreements, the Fund and LAWPRO are liable for such amounts.

7. Members' Levies, Mandatory Insurance Program

Members' levies for the 2004 year include annual base levies of \$2,500 per member (2003 – \$2,500) and additional levies that are charged based on a member's claims history, status, and certain reported transaction volumes. In 2004, additional levies totalled \$26.4 million (2003 – \$26.6 million). The balances are shown net of the retrospective premium rating adjustment.

8. Premium Stabilization Fund

Revenues from transaction based levies are subject to variation in levels of legal transactions that, in part, reflect the changing economic climate. Any revenues from transaction and claims history levies that are in excess of premium levels agreed for the year, are held for future insurance purposes and applied as premiums under the insurance program in future years. Should a shortfall in these levies be experienced, the deficiency in funds shall be transferred from the Premium Stabilization Fund. The amount drawn down in 2004 was nil (2003 – \$6.1 million).

Further, this fund also reflects retrospective premium rate adjustments under the insurance agreement between the Society and LAWPRO. The Premium Stabilization Fund was augmented by \$5.1 million in 2004 through this adjustment (2003 – \$0.7 million).

9. Transfer to Law Society General Fund

Investment income revenues of the stand-alone Fund totalling \$3.0 million (2003 – \$3.0 million), which were determined to be in excess of operating requirements, were transferred to the Society for general purposes.

10. Future Employee Benefits

LAWPRO has a defined contribution pension plan which is available to all its employees. Each employee is required to contribute 4.5% of yearly maximum pensionable earnings and 6% in excess thereof, of an employee's annual base earnings. Under the plan, the Company matches all employee contributions. The Company made payments of \$345,000 in 2004 (2003 – \$322,000) and recorded pension expense of \$353,000 (2003 – \$351,000).

LAWPRO also has a supplemental defined post-retirement benefit plan. Funding of the supplemental plan has not occurred as at the last actuarial valuation date, December 31, 2003. Accordingly, there are no plan assets. For reporting purposes, all assets and liabilities associated with pension benefits or obligations have been measured using values as at December 31, 2004. The following tables describe the Company's commitments and costs for these employee future benefits, presented in accordance with the standards defined in Section 3461 of the CICA Handbook, "Employee Future Benefits."

Errors and Omissions Insurance Fund

| | 2004 (000's) | 2003 (000's) |
|-----------------------------|-----------------|-----------------|
| Accrued benefit obligations | | |
| Balance, beginning of year | 697 | 439 |
| Current service cost | 103 | 58 |
| Interest cost | 69 | — |
| Actuarial loss (gain) | 140 | — |
| Plan amendments | 255 | 200 |
| Balance, end of year | 1,264 | 697 |

The accrued benefit asset (liability) is presented as follows in the balance sheet:

| | | |
|--|---------|-------|
| Included in "Accounts payable and accrued liabilities" | (1,264) | (697) |
|--|---------|-------|

The significant assumptions used by the Company are as follows:

| | |
|--|------------|
| Discount rate | 5.75% |
| Expected long term rate of return on plan assets | 6.00% |
| Rate of compensation increase | 3.50% |
| Estimated average remaining service life | 12.0 years |

The total net expense for the plan was as follows: (000's)

| | |
|---|-----|
| Current service cost | 103 |
| Interest cost | 69 |
| Expected return on plan assets | — |
| Amortization of net actuarial (gain) loss | 140 |
| Amortization of past service costs | 254 |
| Net defined benefit plan expense | 566 |

11. Commitments

LAWPRO is committed to monthly lease payments in effect until January 31, 2008. Lease payment obligations are as follows:

| | |
|------|-------------|
| 2005 | \$1,362,000 |
| 2006 | \$1,362,000 |
| 2007 | \$1,362,000 |
| 2008 | \$ 114,000 |

Management Discussion and Analysis

LibraryCo Inc. is mandated to carry on the central management of the Ontario County and District Law Library system on a not-for-profit basis in accordance with the objectives of the *Blended System* framework for the purpose of developing and enhancing skills for the “competent lawyer” in Ontario.

STATEMENT OF REVENUES AND EXPENSES

LibraryCo experienced a deficit of \$301,000 in 2004 (2003 – \$112,000). The annual deficits were part of budget plans to use LibraryCo’s Reserve Fund as a source of revenue.

Revenues

The \$6.7 million total revenues in 2004 consisted of grants of \$5.9 million (2003 – \$5.7 million) from the Law Society and \$850,000 (2003 – \$850,000) from the Law Foundation of Ontario. The 2004 County Library levy collected by the Law Society was \$197 per member, supplemented by \$220,000 previously collected for County Law Libraries thereby bringing the member rate for 2004 to the equivalent of \$204. The 2003 County Library levy collected by the Law Society was \$195 per member, supplemented by \$323,000 previously collected for County Law Libraries bringing the member rate for 2003 to the equivalent of \$207.

Expenses

Expenses required for the operation of the 48 County and District Law Libraries made up \$6.6 million of the total \$7.1 million. These expenses were primarily for collections – traditional and electronic, personnel and operations. LibraryCo continues to balance the demand for electronic and other materials from the various libraries and to provide education in the use of these materials.

The mix of expenses is consistent with prior years. In 2004, \$416,000 (2003 – \$403,000) was spent on head office operations, the Roving Law Librarian, travel to County and District Law Libraries and administration of the library system.

BALANCE SHEET

There were no significant changes in balance sheet categories or values during the year. The Reserve Fund of \$1.4 million (2003 – \$1.7 million) is restricted for County and District Law Library purposes as approved by the Board of Directors.

Auditors' Report

TO THE SHAREHOLDERS OF LIBRARYCO INC.:

We have audited the balance sheet of LIBRARYCO INC. as at December 31, 2004 and the statements of revenue and expenses, changes in fund balances and cash flows for the year then ended. These financial statements are the responsibility of the organization's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the organization as at December 31, 2004 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

Chartered Accountants

Toronto, Ontario
January 26, 2005

Balance Sheet

*Stated in dollars**As at December 31*

| | 2004 | 2003 |
|---|------------------|------------------|
| CURRENT ASSETS | | |
| Cash and short-term investments | 1,373,689 | 1,652,658 |
| Prepaid expenses | 16,072 | 18,778 |
| Goods and Services Tax receivable | 16,993 | 37,450 |
| | 1,406,754 | 1,708,886 |
| CAPITAL ASSETS (note 4) | 16,514 | 21,957 |
| Total Assets | 1,423,268 | 1,730,843 |
| LIABILITIES, SHARE CAPITAL, AND FUND BALANCES | | |
| Accounts payable and accrued liabilities (note 3) | 27,656 | 34,628 |
| SHARE CAPITAL AND FUND BALANCES | | |
| Share capital (note 5) | 200 | 200 |
| General fund | (13,419) | (17,841) |
| Invested in capital assets fund | 16,514 | 21,957 |
| Reserve fund | 1,392,317 | 1,691,899 |
| Total Share Capital and Fund Balances | 1,395,612 | 1,696,215 |
| Total Liabilities, Share Capital and Fund Balances | 1,423,268 | 1,730,843 |

See accompanying notes

On behalf of the Board of Directors



Chair – Board of Directors



Chair – Finance Committee

Statement of Revenues and Expenses

*Stated in dollars**For the year ended December 31*

| | 2004 | 2003 |
|---|------------------|------------------|
| REVENUES | | |
| Law Society of Upper Canada grant | 5,902,515 | 5,794,650 |
| Law Foundation of Ontario grant | 850,000 | 850,000 |
| Interest income | 20,418 | 40,614 |
| Total revenues | 6,772,933 | 6,685,264 |
| EXPENSES | | |
| Head office/administration | | |
| Salaries and benefits | 193,699 | 210,057 |
| Office and occupancy | 68,212 | 58,295 |
| Professional fees | 53,975 | 50,891 |
| Other (note 6) | 99,692 | 83,652 |
| Total head office/administration expenses | 415,578 | 402,895 |
| County and District Law Libraries – centralized purchases | | |
| Electronic products and services | 1,224,373 | 1,397,039 |
| Insurance and group benefits | 225,903 | 184,380 |
| Other (note 7) | 171,941 | 147,511 |
| | 1,622,217 | 1,728,930 |
| County and District Law Libraries – grants (note 8) | 4,915,678 | 4,605,039 |
| Capital and special needs grants | 120,063 | 60,792 |
| Total County and District Law Libraries expenses | 6,657,958 | 6,394,761 |
| Total expenses | 7,073,536 | 6,797,656 |
| Excess of expenses over revenue for the year | (300,603) | (112,392) |

See accompanying notes

Statement of Changes in Fund Balances

*Stated in dollars**For the year ended December 31*

| | 2004 | | | | 2003 |
|-----------------------------------|-----------------|---------------------------------------|-----------------|------------------|-----------|
| | General Fund | Invested in Capital Assets Fund | Reserve Fund | Total | Total |
| Balance, beginning of year | (17,841) | 21,957 | 1,691,899 | 1,696,015 | 1,808,407 |
| Excess of (expenses over revenue) | | | | | |
| revenue over expenses | (314,285) | (6,736) | 20,418 | (300,603) | (112,392) |
| Purchase of capital assets | (1,293) | 1,293 | — | — | — |
| Inter-fund transfer | 320,000 | — | (320,000) | — | — |
| | (13,419) | 16,514 | 1,392,317 | 1,395,412 | 1,696,015 |

See accompanying notes

Statement of Cash Flows

*Stated in dollars**For the year ended December 31*

| | 2004 | 2003 |
|--|------------------|------------------|
| OPERATING ACTIVITIES | | |
| Excess of expenses over revenue | (300,603) | (112,392) |
| Item not affecting cash | | |
| Amortization of capital assets | 6,736 | 7,644 |
| Net change in non-cash operating working capital items | | |
| Prepaid expenses | 2,706 | (3,474) |
| Goods and Services Tax receivable | 20,457 | 46,371 |
| Due from Law Foundation of Ontario | — | 322,500 |
| Accounts payable and accrued liabilities | (6,972) | (77,220) |
| Total operating activities | (277,676) | 183,429 |
| FINANCING AND INVESTING ACTIVITIES | | |
| Purchase of capital assets | (1,293) | — |
| Increase (decrease) in cash | (278,969) | 183,429 |
| Cash and short-term investments, beginning of year | 1,652,658 | 1,469,229 |
| Cash and short-term investments, end of year | 1,373,689 | 1,652,658 |

See accompanying notes

Notes to Financial Statements

*Stated in whole dollars except where indicated
For the year ended December 31, 2004*

1. General

LibraryCo Inc. (the "organization") was incorporated on April 12, 2001 under the *Ontario Business Corporations Act* as a not-for-profit organization. The Law Society of Upper Canada holds all common shares of the organization and the County and District Law Presidents' Association holds all special shares.

The purpose of the organization is to administer funding from the members of the Law Society of Upper Canada and develop policies, priorities, guidelines and standards for the delivery of county law library services across Ontario including the distribution of funds to the various County and District Law Libraries.

As a not-for-profit organization, LibraryCo Inc. is not subject to federal and provincial income and capital taxes.

2. Significant Accounting Policies

Basis of presentation

The financial statements have been prepared in accordance with the accounting standards for non-profit organizations published by the Canadian Institute of Chartered Accountants, using the restricted fund method of reporting contributions.

The General Fund accounts for the delivery, management and administration of library services. The Reserve Fund is restricted for specific purposes as periodically determined and approved by the Board of Directors. The Invested in Capital Assets Fund records the capital assets of the organization.

Cash and short-term investments

Cash and short-term investments are amounts on deposit and invested in short-term (less than one year) investment vehicles according to the organization's investment policy. Short-term investments are stated at the lower of cost and market value. Investment income, except income earned on General Fund resources, is retained in, and reported by, the Reserve Fund.

Capital assets

Capital assets are presented at cost net of accumulated amortization. Amortization is charged to expenses on a declining balance basis as follows:

| | |
|------------------------|----------------------------------|
| Furniture and fixtures | 20% |
| Computer equipment | 30% |
| Leasehold improvements | Straight-line over term of lease |

In the year of acquisition, half the normal amortization is provided.

Computer software is expensed in the year of acquisition.

Revenue recognition

Restricted contributions related to the general operations are recognized as revenue of the General Fund in the year in which the related expenses are incurred. All other restricted contributions are recognized as revenue of the appropriate restricted fund.

Collections

The organization owns a collection of traditional, and electronic-based, legal research and reference material. The cost of additions to the collection is expensed as incurred.

Financial instruments

The estimated fair value of cash and short-term investments, accounts receivable, prepaid expenses, accounts payable and accrued liabilities approximate their carrying amounts in the financial statements due to the relatively short period to maturity of these instruments.

Measurement uncertainty

The preparation of the financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingencies at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

3. Related Party Transactions and Balances

| | 2004 | 2003 |
|---|-----------|-----------|
| <i>Transactions</i> | | |
| Purchases from the Law Society of Upper Canada | \$ 96,831 | \$ 93,292 |
| <i>Balances</i> | | |
| Amount due to the Law Society of Upper Canada (included in accounts payable and accrued liabilities) | \$ - | \$ 7,680 |

Included in purchases from the Law Society of Upper Canada are costs associated with cataloguing of collections, post-call programs and Bar Admission Course materials for the County and District Law Libraries and catering for Board of Directors' meetings.

4. Capital Assets

| | 2004 | | | 2003 |
|------------------------|----------|--------------------------|----------|----------|
| | Cost | Accumulated amortization | Net | Net |
| Furniture and fixtures | \$16,563 | \$ 9,115 | \$ 7,448 | \$ 9,180 |
| Computer equipment | 20,630 | 14,242 | 6,388 | 8,314 |
| Leasehold improvements | 8,927 | 6,249 | 2,678 | 4,463 |
| | \$46,120 | \$29,606 | \$16,514 | \$21,957 |

5. Share Capital

Authorized

Unlimited number of Common shares

Unlimited number of Special shares, with right to elect one director

| Issued | 2004 | 2003 |
|--------------------|--------------|-------|
| 100 Common shares | \$100 | \$100 |
| 100 Special shares | 100 | 100 |
| | \$200 | \$200 |

At incorporation, the organization issued 100 Common shares to the Law Society of Upper Canada and 100 Special shares to the County and District Law Presidents' Association for cash consideration of \$100 each.

6. Other Expenses – Head Office/Administration

Included in this expense are costs associated with staff travel, Board of Directors' meetings and other miscellaneous items.

7. Other Expenses – County and District Law Libraries – Centralized Purchases

Included in this expense are costs associated with publications, cataloguing, committee meetings, and other miscellaneous items.

8. County and District Law Library Grants

These grants represent the quarterly distribution of funds to the 48 County and District Law Libraries. These grants are distributed in accordance with policies and procedures as established by the organization's Board of Directors.

In order to satisfy themselves as to the proper use of these funds, management has undertaken the following procedures:

Periodic visits, by the organization's staff, to the individual libraries to review financial information, assess collections, and to determine services being provided;

Submission of annual budgets by each individual library and review of these budgets by the organization's staff;

Submission of periodic financial information by each individual library and review of this information by the organization's staff;

Annual conference with the organization's staff and staff of all individual libraries.

The following individual library grants were distributed by the organization during 2004 and 2003:

| | 2004 | 2003 |
|--|--------------------|--------------------|
| Algoma District Law Association | \$ 104,952 | \$ 71,000 |
| Brant Law Association | 67,404 | 62,000 |
| Bruce Law Association | 50,012 | 45,600 |
| County of Carleton Law Association | 536,160 | 483,000 |
| Cochrane Law Association | 38,960 | 55,000 |
| Dufferin Law Association | 43,428 | 42,200 |
| Durham County Law Association | 101,992 | 96,000 |
| Elgin Law Association | 59,584 | 52,200 |
| Essex Law Association | 212,788 | 204,160 |
| Frontenac Law Association | 117,952 | 108,000 |
| Grey Law Association | 51,892 | 52,000 |
| Haldimand Law Association | 23,256 | 34,500 |
| Halton Law Association | 103,592 | 97,900 |
| Hamilton Law Association | 333,906 | 286,000 |
| Hastings Law Association | 66,956 | 64,000 |
| Huron Law Association | 58,688 | 56,000 |
| Kenora Law Association | 69,012 | 62,000 |
| Kent Law Association | 55,912 | 44,000 |
| Lambton County Law Association | 48,811 | 46,000 |
| County of Lanark Law Association | 36,292 | 34,000 |
| Leeds & Grenville Law Association | 53,456 | 48,000 |
| Lennox & Addington Law Association | 21,892 | 21,000 |
| Lincoln Law Association | 129,807 | 125,500 |
| Manitoulin Law Association | 6,000 | 5,500 |
| Middlesex Law Association | 271,532 | 260,000 |
| Muskoka Law Association | 39,108 | 37,000 |
| Nipissing Law Association | 63,920 | 57,000 |
| Norfolk Law Association | 55,480 | 49,000 |
| Northumberland County Law Association | 55,464 | 47,368 |
| Oxford Law Association | 58,536 | 54,000 |
| Parry Sound Law Association | 24,180 | 30,000 |
| Peel Law Association | 217,425 | 225,000 |
| County of Perth Law Association | 51,452 | 42,000 |
| Peterborough Law Association | 86,274 | 78,000 |
| Prescott & Russell Law Association | 11,439 | 33,000 |
| Rainy River Law Association | 22,280 | 38,000 |
| Renfrew County Law Association | 90,612 | 85,000 |
| County of Simcoe Law Association | 120,596 | 115,000 |
| Stormont, Dundas & Glengarry Law Association | 59,112 | 54,000 |
| Sudbury District Law Association | 123,060 | 109,000 |
| Temiskaming Law Association | 40,144 | 39,000 |
| Thunder Bay Law Association | 124,944 | 120,000 |
| Toronto Lawyers Association | 467,388 | 459,000 |
| Victoria Haliburton Law Association | 65,800 | 58,000 |
| Waterloo Law Association | 188,992 | 170,611 |
| Welland Law Association | 70,700 | 65,000 |
| Wellington Law Association | 62,020 | 59,500 |
| York Region Law Association | 152,516 | 125,000 |
| | <u>\$4,915,678</u> | <u>\$4,605,039</u> |

9. Lease Commitments

The organization has entered into a lease arrangement for its offices. The lease term is five years, expiring July 31, 2006 and requires annual payments of \$10,992 plus operating costs for the first three years and \$13,200 plus operating costs for the last two years.

10. Contingencies and Guarantees

In the normal course of business, the organization enters into agreements that meet the definition of a guarantee. The organization's primary guarantees are as follows:

(a) Indemnity has been provided to all directors and/or officers of the organization for various items including, but not limited to, all costs to settle suits or actions due to their involvement with the organization, subject to certain restrictions. The organization has purchased directors' and officers' liability insurance to mitigate the cost of any potential future suits or actions. The term of the indemnification is not explicitly defined, but is limited to the period over which the indemnified party served as a trustee, director or officer of the organization. The maximum amount of any potential future payment cannot be reasonably estimated.

(b) In the normal course of business, the organization has entered into agreements that include indemnities in favour of third parties, such as purchase and sale agreements, engagement letters with advisors and consultants, leasing contracts, information technology agreements and service agreements. These indemnification agreements may require the organization to compensate counterparties for losses incurred by the counterparties as a result of breaches in representation and regulations or as a result of litigation claims or statutory sanctions that may be suffered by the counterparty as a consequence of the transaction. The terms of these indemnities are not explicitly defined and the maximum amount of any potential reimbursement cannot be reasonably estimated.

The nature of these indemnification agreements prevents the organization from making a reasonable estimate of the maximum exposure due to the difficulties in assessing the amount of liability which stems from the unpredictability of future events and the unlimited coverage offered to counterparties. Historically, the organization has not made any significant payments under such or similar indemnification agreements and therefore no amount has been accrued in the financial statements with respect to these agreements.

11. Comparative Figures

Certain prior year amounts have been reclassified to conform to the current year's presentation.



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